12 Mar 2019

Securities Analysis

Equity Research

Ping An Bank (000001 CH)

Takeaways from retail banking corporate day

- We attended Ping An Bank's (PAB) retail banking corporate day in Shenzhen last week. We see tremendous growth potential for the Bank's retail business, as it benefits from Ping An Group's all-rounded supports and successful migration of client base.
- **In the second stage of retail transformation.** PAB officially kicked off its retail transformation in 2H16, with the foremost target of growing retail client base (40.5 mn in FY16) and lifting retail revenue contribution (30.6% in FY16). By end-FY18, no. of client and proportion of revenue from retail segment reached 83.9 mn and 53%, respectively. Since 4Q18, PAB has entered the second stage of retail transformation (Figure 1), with key objective of enhancing earnings ability. A major initiative is to boost private banking and wealth management businesses.
- **The core "3+2+1" framework.** PAB's retail business is underpinned by a unique framework (Figure 2), which comprises: three modules - basic retail, consumer finance & private banking (PB); two competencies - cost & risk management; and one internal driver - Artificial Intelligence (AI). Basic retail mainly supports customer acquisition and volume growth, while consumer finance and PB are major profit and AUM generators.
- **Comparison with "Industry benchmark".** CMB (600036 CH, NR) is broadly recognized as the best retail bank in China. As such, we compare PAB to CMB on multiple fronts of retail business, including 1) revenue & profit mix; 2) structure & pricing of loans & deposits; 3) NPL ratio; 4) client amount & AUM per capita, and 5) cost-income ratio. We found that PAB is comparable to CMB in retail profit and loan contribution, but inferior in operating efficiency, asset quality and profitability.
- **4Q18 results highlights.** A bright spot was 13bps QoQ NIM expansion, which drove a 15.8% YoY revenue growth in 4Q18. Despite the 41% YoY surge in impairment charges, net profit still saw a decent growth of 7.0% YoY, beating most joint-stock peers. It was also encouraging to see a notable increase in the Bank's NPL/90-day overdue ratio (up 22ppts QoQ to 103%), which has been a valuation overhang in past years. Stricter NPL recognition will ease regulatory risks and further unleash PAB's earnings momentum ahead. A major weakness was the Bank's thin capital buffer, as CET-1 CAR only stood at 8.54% (vs 7.5% threshold) in 4Q18.
- **Valuation.** PAB currently trades at 0.85x FY19E P/B, vs 0.87x for A-share bank average and 1.34x for CMB-A. There is foreseeable valuation upside, should the Bank's retail strategy leads to improving financial performance in coming years. PAB is also a key beneficiary of further RRR cuts.

Earnings summary

(YE 31 Dec)	FY16A	FY17A	FY18A
Operating income (RMB mn)	107,715	105,786	116,716
Net profit (RMB mn)	22,599	23,189	24,818
EPS (RMB)	1.44	1.30	1.39
EPS CHG (%)	(7.7)	(9.5)	7.3
P/B (x)	1.16	1.05	0.96
P/E (x)	8.6	9.5	8.8
Yield (%)	1.3	1.1	1.2
ROAE (%)	13.1	11.6	11.3
NPL (%)	1.74	1.70	1.75
Allowance/ NPLs (%)	155.4	151.1	155.2

Source: Company data, CMBIS

NOT RATED

Current Price	RMB 12.32

Terry Sun, CFA
Tel: (852) 3900 0836
Email: terrysun@cmbi.com.hk

Karen Sui
Tel: (852) 3761 8775
Email: suixiaomeng@cmbi.com.hk

China Banking Sector

Mkt. Cap. (RMB mn)	211,539
Avg. 3mths t/o (RMB mn)	1,087.40
52W High/Low (RMB)	13.38/8.45
Total Issued Shares (mn)	17,170.4

Source: Bloomberg

Shareholding Structure

Ping An Insurance (Grp)	49.56%
Ping An Life Insurance	8.38%
CSFC	2.50%

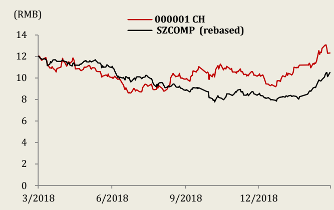
Source: Bloomberg

Share Performance

	Absolute	Relative
1-mth	9.8%	-10.4%
3-mth	20.9%	0.4%
6-mth	24.5%	9.1%

Source: Bloomberg

12-mth Price Performance



Source: Bloomberg

Auditor: PwC
Web-site: bank.pingan.com

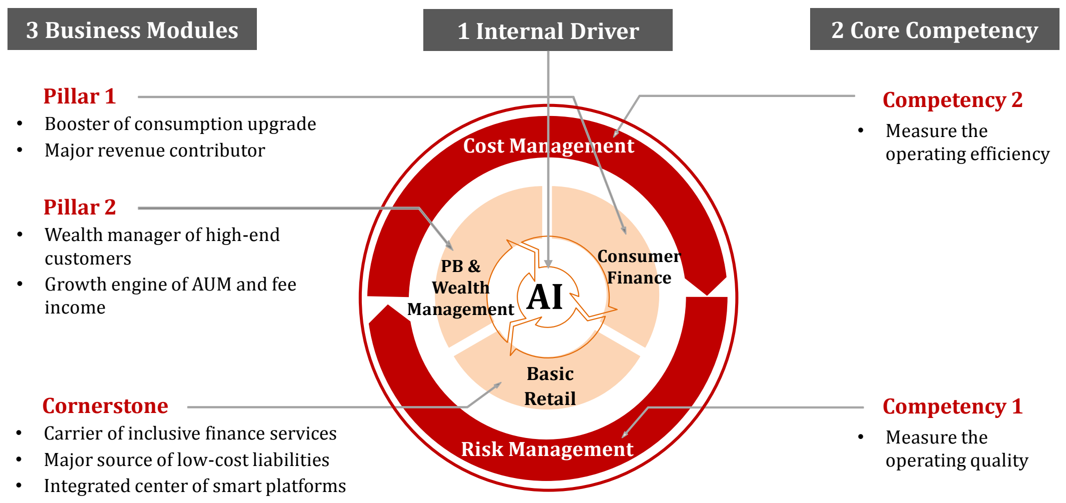
Overview of PAB's retail banking strategy

Figure 1: Progress of PAB's retail transformation

	Stage 1	Stage 2	Stage 3
Timeline	2017 - 2018	2019	2020 & beyond
Business focus	- Invest in technology and infrastructure - Grow client base - Improve user experience	- Broaden the application of technology - Increase customer satisfaction and loyalty - Enhance value creation and boost profit	- Business model innovation led by technology - Establish brand reputation and franchise - Full-scale financial performance
Key initiatives	- Increase credit allocation to retail (esp. credit cards, consumer loans and car loans); - Reduce corporate loan scale, focus on selective industries, and develop asset- & capital-light business; - Create "Online Merge Offline (OMO)" business model, through mobile APP, smart outlets & SAT services; - Leverage on group resources	- Merge wealth management team of Ping An Trust into private banking division; - Use AI in customer acquisition/marketing/customer services/management; - Develop smart platform for Xin Yi Dai and auto finance; - Build cost management system to monitor the cost saving effect from AI utilization	NA

Source: Company data, CMBIS

Figure 2: PAB's retail business framework



Source: Company data, CMBIS

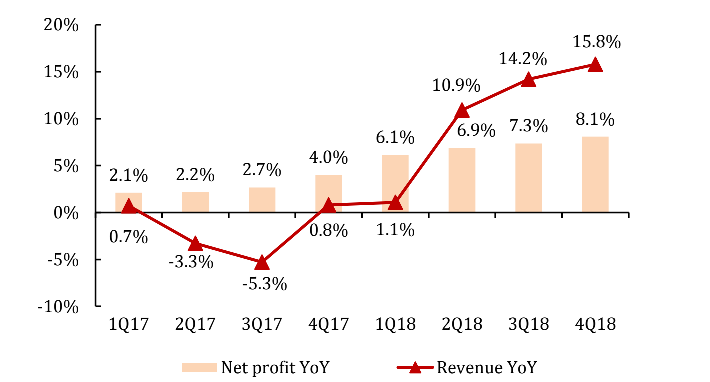
4Q18 operating results

Figure 3: Results summary

(RMB mn)						
P&L	**FY17**	**FY18**	**YoY**	**4Q17**	**4Q18**	**YoY**
Net interest income	74,009	74,745	1.0%	18,527	20,216	9.1%
Net fee and commission income	30,674	31,297	2.0%	7,513	7,592	1.1%
Operating income	**105,786**	**116,716**	**10.3%**	**25,954**	**30,052**	**15.8%**
Operating expense	(32,638)	(36,540)	12.0%	(10,625)	(10,112)	-4.8%
PPoP	**73,148**	**80,176**	**9.6%**	**15,329**	**19,940**	**30.1%**
Impairment losses	(42,925)	(47,871)	11.5%	(10,105)	(14,249)	41.0%
Operating profit	**30,223**	**32,305**	**6.9%**	**5,224**	**5,691**	**8.9%**
Income tax	(6,968)	(7,413)	6.4%	(1,182)	(1,303)	10.2%
Net profit	**23,189**	**24,818**	**7.0%**	**4,036**	**4,362**	**8.1%**
Balance sheet	**FY17**	**FY18**	**YoY**	**3Q18**	**4Q18**	**QoQ**
Gross loans	1,704,230	1,997,529	17.2%	1,922,047	1,997,529	3.9%
Customers' deposits	2,000,420	2,149,142	7.4%	2,134,641	2,149,142	0.7%
Total assets	3,248,474	3,418,592	5.2%	3,352,056	3,418,592	2.0%
NPLs	28,997	34,905	20.4%	32,245	34,905	8.2%
Key ratios	**FY17**	**FY18**	**YoY**	**3Q18**	**4Q18**	**QoQ**
ROE	11.6%	11.3%	-0.3ppt	13.4%	8.0%	-5.4ppt
NPL ratio	1.70%	1.75%	5bp	1.68%	1.75%	7bp
Provision coverage	151.1%	155.2%	4.2ppt	168.8%	155.2%	-13.6ppt
LDR	85.2%	92.9%	7.8ppt	90.0%	92.9%	2.9ppt
CET-1 CAR	8.3%	8.5%	26bp	8.5%	8.5%	0bp

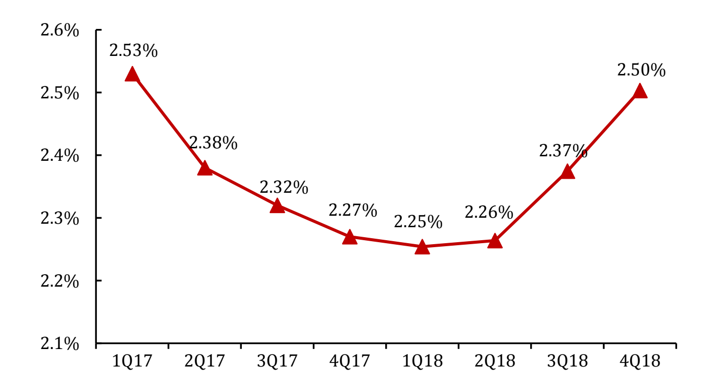
Source: Company data, CMBIS

Figure 4: Revenue and net profit growth



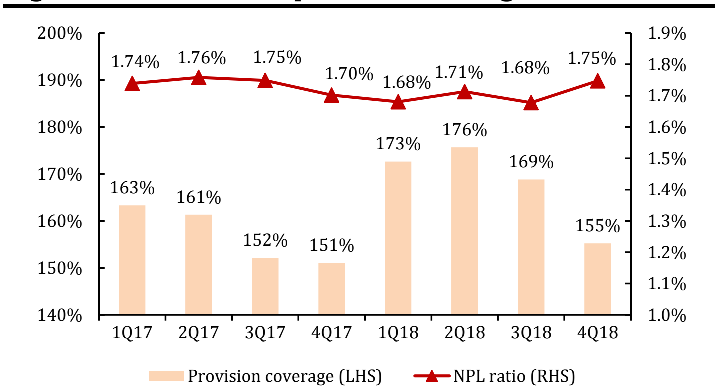
Source: Company data, CMBIS

Figure 5: Quarterly NIM



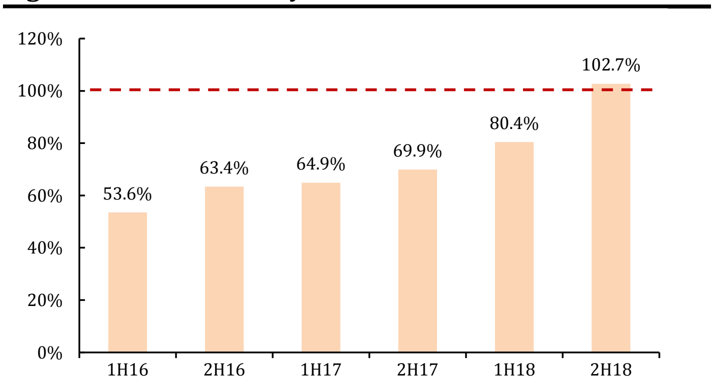
Source: Company data, CMBIS

Figure 6: NPL ratio and provision coverage



Source: Company data, CMBIS

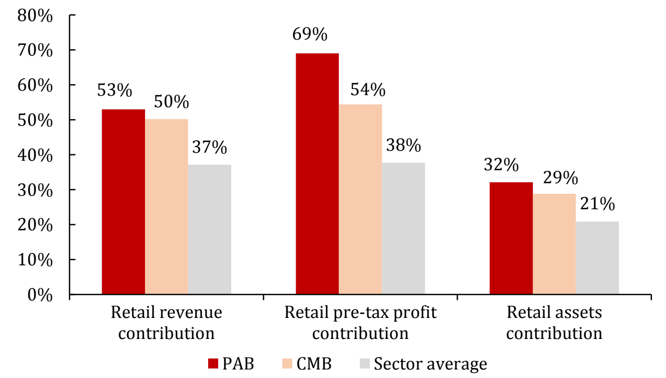
Figure 7: NPL to >90-day overdue loans



Source: Company data, CMBIS

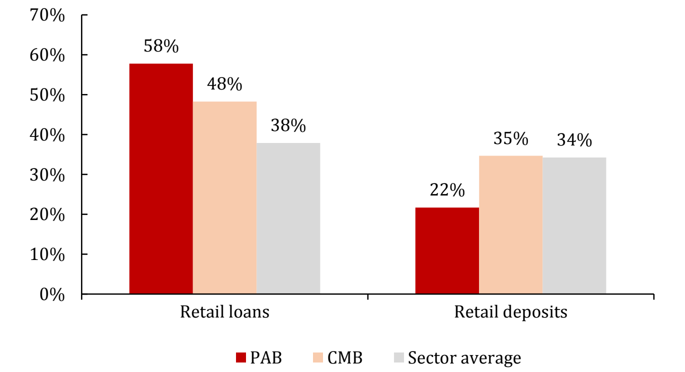
Peer comparison

Figure 8: Retail business contribution



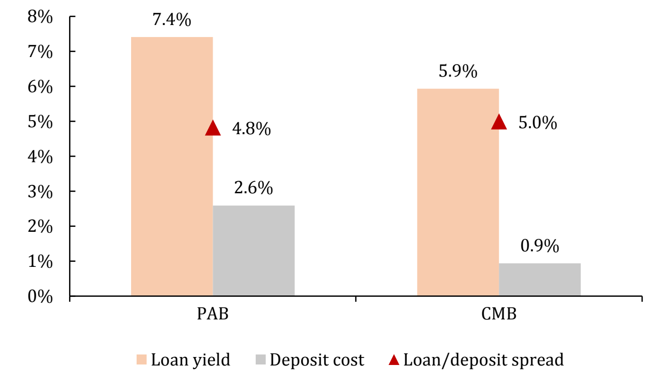
Source: Company data, CMBIS
Note: 2018 data for PAB and 1H18 data for other banks.

Figure 9: Retail loan and deposit contribution



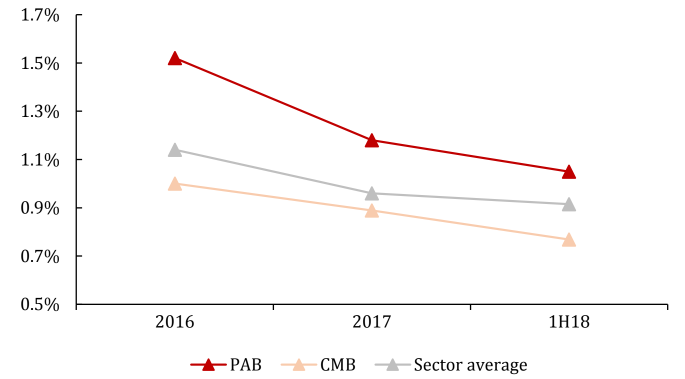
Source: Company data, CMBIS
Note: 2018 data for PAB and 1H18 data for other banks.

Figure 10: Loan yield and deposit cost in 1H18



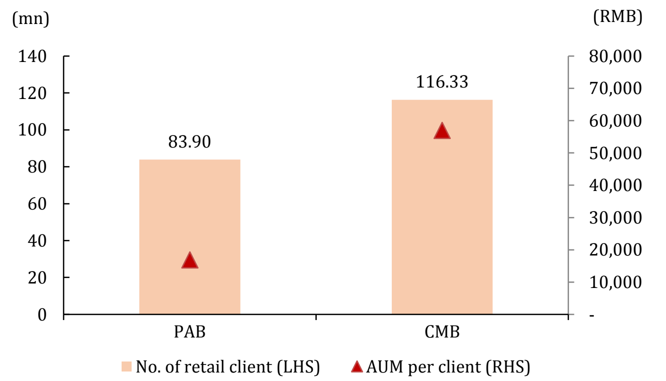
Source: Company data, CMBIS

Figure 11: NPL of retail loans



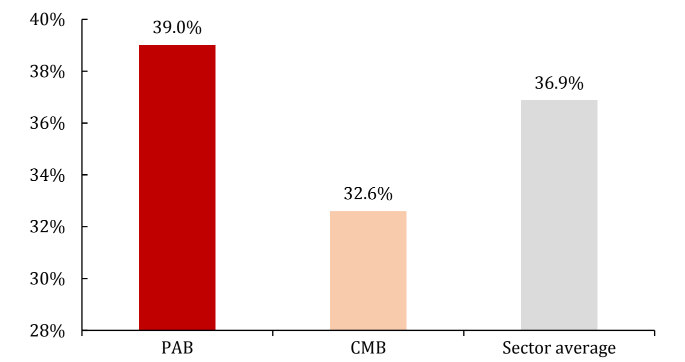
Source: Company data, CMBIS

Figure 12: No. of retail clients and retail AUM



Source: Company data, CMBIS
Note: 2018 data for PAB and 1H18 data for CMB.

Figure 13: Retail business cost-income ratio in 1H18



Source: Company data, CMBIS

Financial statements

Income statement

Year ended: 31 Dec (RMB mn)	2016	2017	2018
Interest income	131,119	148,068	162,888
Interest expenses	(54,708)	(74,059)	(88,143)
Net interest income	**76,411**	**74,009**	**74,745**
Net fee and commission income	**27,859**	**30,674**	**31,297**
Other gains and income	3,445	1,103	10,674
Operating income	**107,715**	**105,786**	**116,716**
Operating expenses	(31,418)	(32,638)	(36,540)
PPoP	**76,297**	**73,148**	**80,176**
Impairment losses	(46,518)	(42,925)	(47,871)
Operating profit	**29,779**	**30,223**	**32,305**
Non-operating income	156	(66)	(74)
Pre-tax profit	**29,935**	**30,157**	**32,231**
Income tax expenses	(7,336)	(6,968)	(7,413)
Profit for the year	**22,599**	**23,189**	**24,818**
Non-controlling interests	0	0	0
Net profit	**22,599**	**23,189**	**24,818**

Source: Company data, CMBIS

Balance statement

Year ended: 31 Dec (RMB mn)	2016	2017	2018
Due from central banks	306,763	305,986	273,513
Interbank assets	273,208	231,157	195,017
Investments	759,438	807,002	850,317
Loans and advances, net	**1,435,869**	**1,660,420**	**1,949,757**
Other assets	178,156	243,909	149,988
Total assets	**2,953,434**	**3,248,474**	**3,418,592**
Due to central banks	19,137	130,652	149,756
Interbank liabilities	697,227	762,663	725,461
Customer deposits	**1,921,835**	**2,000,420**	**2,149,142**
Debt securities issued	30,115	45,116	81,755
Other liabilities	82,949	87,569	72,436
Total liabilities	**2,751,263**	**3,026,420**	**3,178,550**
Total shareholders' equity	**202,171**	**222,054**	**240,042**
Non-controlling interests	0	0	0
Total equity	**202,171**	**222,054**	**240,042**

Source: Company data, CMBIS

Key ratios

Year ended: 31 Dec	2016	2017	2018
Operating income mix			
Net interest income	71%	70%	64%
Net fee and commission income	26%	29%	27%
Other gains and income	3%	1%	9%
Total	**100%**	**100%**	**100%**
Growth			
Net interest income	11.6%	-3.1%	1.0%
Net fee and commission income	15.7%	10.1%	2.0%
Operating income	**12.0%**	**-1.8%**	**10.3%**
Operating expenses	-14.6%	3.9%	12.0%
PPoP	28.5%	-4.1%	9.6%
Net profit	**3.4%**	**2.6%**	**7.0%**
Asset quality indicators			
Non-performing loan ratio	1.74%	1.70%	1.75%
Provision coverage ratio of NPLs	155.37%	151.08%	155.24%
Provision to total loans	2.71%	2.57%	2.70%
Credit costs	3.38%	2.57%	2.36%
Capital adequacy ratio			
Common equity tier 1 CAR	8.36%	8.28%	8.54%
Tier 1 CAR	9.34%	9.18%	9.39%
CAR	11.53%	11.20%	11.50%
Returns			
ROAE	13.15%	11.61%	11.34%
ROAA	0.83%	0.75%	0.74%
Per share			
EPS (RMB)	1.44	1.30	1.39
DPS (RMB)	0.16	0.14	0.15
BVPS (RMB)	10.61	11.77	12.82

Source: Company data, CMBIS

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CMB International Securities Limited

Address: 45th and 46th Floor, Champion Tower, 3 Garden Road, Hong Kong Tel: (852) 3900 0888 Fax: (852) 3900 0800

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